Economics 296 B: Senior Seminar-exchange rate economics with reference to selected Arab countries

Jan. 2006 **Final Examination** **Two hours**

Answer question 5 and any <u>three</u> of the remaining four questions:

(22%) 1. Suppose a certain country is suffering from persistent balance of payment deficits due to excessive domestic spending. Discuss some of the policy measures that can be taken to address or correct this situation.
In answering this question keep in mind the analytic definition of a deficit and the interrelationships between national and international accounts.

(22%)2. Take the elasticity approach.

(a) What are its underlying assumptions?

(b) Discuss the conditions under which a devaluation of the national currency would improve the balance of payment or more specifically the current account.

(22%)3.Take the absorption approach. Discuss how a devaluation of the national currency leads to an improvement in the current account.

(22%) 4.Consider the common features of developing countries (e.g., dependence on markets of industrial countries, limited development of domestic financial markets, reliance on foreign direct investment and other capital inflows to promote growth etc.), Do you think a flexible exchange rate policy would be preferable for them than a policy of a pegged exchange rate? Discuss.

(34 %) 5. Take the Lebanese case. Assess the exchange rate policy that has been followed since late 1992 (pegging to the US dollar). Do you think it was the appropriate policy to follow? What are some of its advantages (if any) and disadvantages (if any).
In answering the question keep in mind the evolving macro-economic background and the major objective(s) of the exchange rate policy.

Please number your pages and try to write legibly.